

SOUTHERN UNION EXPLORATION CO.

IBLA 85-457

Decided May 20, 1987

Appeal from a decision of the New Mexico State Office, Bureau of Land Management, rejecting high bid for competitive oil and gas lease NM-60339.

Affirmed.

1. Oil and Gas Leases: Competitive Leases -- Oil and Gas Leases:
Discretion to Lease

The Secretary of the Interior has the discretionary authority to reject a high bid in a competitive oil and gas lease sale when the record discloses a rational basis for the conclusion that the amount of the bid was inadequate. The explanation provided must inform the bidder of the factual basis of the decision and must be sufficient for the Board to determine the correctness of the decision if disputed on appeal.

2. Oil and Gas Leases: Competitive Leases -- Oil and Gas Leases:
Discretion to Lease

The Department is entitled to rely on the reasoned analysis of its technical experts in matters concerning geologic evaluation of tracts of land offered at a sale of competitive oil and gas leases. When an appellant fails to meet its affirmative obligation to establish that its bid is a reasonable reflection of fair market value, a decision by BLM to reject a bid will be sustained.

APPEARANCES: Dennis K. Morgan, Esq., Assistant General Attorney, Southern Union Exploration Company, for appellant.

OPINION BY ADMINISTRATIVE JUDGE FRAZIER

The Southern Union Exploration Company has appealed from a February 12, 1985, decision of the New Mexico State Office, Bureau of Land Management (BLM), rejecting its high bid for competitive oil and gas lease NM-60339. Appellant was the high bidder for parcel 6, in the October 25, 1984, competitive oil and gas lease sale. Appellant had submitted a bid of \$ 15,925.85 (\$ 51.47/acre), for the parcel, which consists of 309.42 acres of land situated in lots 5

through 8 and the SW 1/4 sec. 5, T. 31 N., R. 13 W., New Mexico Principal Meridian, San Juan County, New Mexico.

By memorandum dated November 2, 1984, the Deputy State Director, Mineral Resources, advised the Deputy State Director, Operations, that the Southwest Region Evaluation Team (SRET) had recommended rejection of appellant's bid. On November 21, 1984, BLM issued a notice informing appellant that its bid was lower than the presale estimate of value (PEV) assigned to the parcel and that it was being considered for rejection. BLM did not disclose its PEV but afforded appellant an opportunity to provide information to establish that its bid was reasonable and should not be rejected. BLM gave appellant 15 days from receipt of the notice to file the information, and advised: "If no information is submitted, a decision will be issued rejecting your bid."

By memorandum dated February 1, 1985, the Acting Chief, SRET, notified the Chief, Mineral Leasing Unit 1, that appellant had "not responded" to the November 1984 notice and recommended rejection of appellant's bid because appellant had failed to respond timely and because the bid was "substantially below" the SRET presale appraised value of the parcel, i.e., \$ 30,000. The memorandum stated that SRET had "used a 'Monte Carlo' discounted cash flow (DCF) analysis and a study of recent comparable area lease sales to determine the presale appraised value." The memorandum stated that "[d]ocumentation of this information is being maintained in the SRET files." BLM issued its February 1985 decision stating: "By notice of Nov. 21, 1984, you were allowed the opportunity to provide this office with information as to why your bid should be considered reasonable and not be rejected. This information was not submitted within the 15-day period. Therefore, your bid is hereby rejected." 1/ BLM included a copy of the SRET report with its decision.

Appellant filed its notice of appeal and requested BLM to provide within 15 days the "[d]ocumentation" alluded to in the February 1985 memorandum, which BLM used in arriving at its presale appraised value, "in order that [appellant] may evaluate and incorporate the same in its Statement of Reasons for Appeal." In its statement of reasons filed March 13, 1985, appellant states that in response to its request for the supporting documentation, BLM, on February 28, 1985, advised appellant by telephone that the information was confidential and "thus could not be furnished" by BLM. 2/ Appellant states that it was directed to make its request to the Board. On appeal, appellant asks the Board to set aside the February 1985 BLM decision and to remand the case to BLM for a "readjudication" of appellant's bid, because BLM has provided no information, other than the presale appraised value, to support its decision.

1/ While the decision might be read to say that appellant's bid was rejected because of its failure to submit additional information, clearly it was the determination that appellant's high bid was below the PEV that was the basis for the rejection.

2/ Nothing in the case file has been given confidential designation, however.

The record shows that the information originally requested by appellant was included in the case file after the decision was issued. In a routing and transmittal slip from the Minerals Division, dated March 15, 1985, SRET states: "Attached is the original evaluation for Parcel #6 on the 10/25/84 KGS lease sale; NM 60339. This together with previous data should complete the file for submitting to [the Board]." This evaluation apparently consists of a summary sheet, well location and structural contour maps, data entered in the DCF analysis and comparable lease data. There is also a post sale notice, dated March 15, 1985, indicating the results of a December 1984 competitive oil and gas lease sale of a contiguous parcel which received a high bid of \$ 150.09 per acre.

Since copies of this evaluation and data had not been provided to appellant, the Board, by order of June 27, 1986, directed BLM to furnish copies of the documents to appellant, and granted appellant 30 days from receipt thereof in which to file a response. Appellant received this information on July 7, 1986. However, it did not file a response with the Board.

The tract evaluation of parcel 6 dated October 24, 1984, states:

The subject parcel is [a] 309.420 acre tract in San Juan County, New Mexico; being Lots 5 thru 8 inclusive and the SW/4 of Section 5, T31N, R13W; NMPM. The known geological structure (KGS) is the "San Juan-Defined," and the producing areas involved are known as the "Ute Dome Field" and the "La Plata Gallup Field."

Historically the "Ute Dome" has proven gas production from the "Dakota" formation of the Cretaceous at depths in the 2,000' range, and the main pay zone is the "Paradox" formation (Barker Creek member) of the Pennsylvanian at depths in the 7,500' range. The "La Plata Gallup" has a long history of oil and gas production from the "Mancos Shale" of the Cretaceous at depths in the 6,000' range. The subject tract is felt to be strongly influenced by the potential related to the "La Plata Gallup" with some possible influence from the "Ute Dome" (maps attached).

Specifically, the subject tract has been previously leased, and with an oil well with a bottom hole location in the extreme southeast corner it has produced over 345,000 bbls. of oil from the "La Plata Gallup" before being abandoned. All the data available to this office indicates that there are no structural or stratigraphic anomaly conditions between the south portion and the north portion of the subject. On the basis of the published geology and production histories (see attached), it is estimated that there is a 50% possibility (50% risk) of obtaining a "La Plata" oil well on the north portion of the subject with potential reserves ranging between 25,000 and 45,000 barrels, with a most probable estimate of 30,000 barrels. Using the 50% risk and reserve estimation as stated, a "Monte Carlo" Discounted Cash Flow with 5,000 iterations was performed using the "PWI" model.

Well completion costs, dry hole costs, and other parameters available and used by industry were input data into the model. The result was a value for bonus for the subject of \$ 33,431.67 or \$ 108.05/acre. For the purpose of this valuation, this amount was rounded to \$ 30,000.00 (see attached "PWI" printout).

Recent comparable lease sales in adjoining townships indicate a range of from \$ 75.00 per acre to \$ 200.00 per acre for tracts with relatively similar geologic and production potential; therefore, the value estimate derived from "PWI" is within the market bracket.

Estimated market value for bonus for this tract as of 10/25/84 is: \$ 30,000.00.

[1] The Secretary of the Interior has discretionary authority to reject a high bid for a competitive oil and gas lease as inadequate. 30 U.S.C. § 226(b) (1982); see, e.g., Michael Shearn, 87 IBLA 168, 169 (1985); Viking Resources Corp., 80 IBLA 245 (1984). This Board has consistently upheld that authority, so long as there is a rational basis for the conclusion that the highest bid does not represent fair market value for the parcel. E.g., Clarence Sherman, 82 IBLA 64, 65 (1984); Viking Resources Corp., supra at 246; Glen M. Hedge, 73 IBLA 377, 378-79 (1983). Departmental policy in the administration of its competitive leasing program is to seek the return of fair market value for the grant of leases, and the Secretary reserves the right to reject a bid which will not provide a fair return. Viking Resources Corp., supra at 246; Glen M. Hedge, supra at 379; Coquina Oil Corp., 29 IBLA 310, 311 (1977).

[2] The Department is entitled to rely on the reasoned analysis of its technical experts in matters involving geologic evaluation of tracts of land offered at a sale of competitive oil and gas leases. Viking Resources Corp., supra at 247; L. B. Blake, 67 IBLA 103 (1982). However, when BLM relies on that analysis in rejecting a bid as inadequate, it must ensure that a reasoned explanation is provided in the record to support the decision. E.g., Mesa Petroleum Co., 81 IBLA 194, 195 (1984); Edward L. Johnson, 73 IBLA 253, 255 (1983). Otherwise, if the bid is not clearly spurious or unreasonable on its face, the Board has consistently held that the decision must be set aside and the case remanded for compilation of a more complete record and readjudication of the acceptability of the bid. E.g., Kevin J. Bliss, 82 IBLA 31, 32 (1984); Mesa Petroleum Co., supra at 195.

The critical question, then, is whether BLM has provided a reasoned explanation for its rejection of appellant's high bid for parcel 6. The PEV of the parcel was \$ 30,000 (\$ 96.96 per acre) and appellant's high bid of \$ 15,925.85 (\$ 51.47 per acre) was deemed substantially below the BLM presale estimate. After considering the entire record, we find that on appeal BLM established a rational basis for its PEV. The decision was based on the use of a "Monte Carlo"-type of a discounted cash flow (DCF) analysis in association with a study of recent comparable area lease sales to determine the

presale appraised value. Industry-accepted parameters for drilling costs, taxes, operating costs, reserve estimates, etc., were used as the inputs into DCF, and 5,000 runs were made. The DCF results were "risk-weighted," and from this a final value was established for the presale appraisal. Further, the high bid for the lease near parcel 6 received in December 1984 supports BLM's position that its PEV is a reasonable estimate of the fair market value.

This documentation was eventually provided to appellant, and appellant was afforded an opportunity to present its own geologic data and analysis to show that its bid was reasonable. ^{3/} Appellant has an affirmative obligation to demonstrate that the Government estimate is inaccurate and that its bid represents the fair market value. The Westlands Co., 83 IBLA 43 (1984). The Secretary or his delegate need not prove appellant's bid inadequate in order to support a rejection decision. A rejection is an exercise of the Secretary's discretion, and deference is given to such action if, in the public interest, the Secretary determines a bid to be for less than the Department's estimate of fair market value. The record need only be sufficient to establish that the decision was neither arbitrary nor capricious. Harvey E. Yates Co., 71 IBLA 134 (1983); Kerr McGee Corp., 6 IBLA 108 (1972), aff'd, Kerr McGee Corp. v. Morton, 527 F.2d 838 (D.C. Cir. 1975). Appellant has not presented any evidence to show that BLM's PEV is not correct.

Accordingly, we find the record supports the rejection of appellant's bid. Appellant has made no showing that the decision was arbitrary, capricious or based upon inaccurate data. Appellant has failed to establish that the Government's evaluation was erroneous.

Therefore, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision appealed from is affirmed.

Gail M. Frazier
Administrative Judge

We concur:

Kathryn A. Lynn
Administrative Judge
Alternate Member

R. W. Mullen
Administrative Judge

^{3/} This case illustrates the need to disclose the basis for rejection at the earliest practicable date. Had the information ultimately furnished to appellant at the direction of this Board been submitted with the initial notice, appellant may have been satisfied with BLM's basis for rejection and not filed an appeal, thus avoiding the cost in time and Federal funds resulting from our consideration of this matter. We strongly urge BLM to submit the information to the bidding party at the time of notice of intent to reject.